



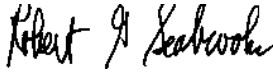
**U.S. SMALL BUSINESS ADMINISTRATION
OFFICE OF INSPECTOR GENERAL
WASHINGTON, D.C. 20416**

AUDIT REPORT
Issue Date: March 30, 2000
Number: 0-14

To: Robert Baskin
Associate Administrator for Field Operations

Jane Palsgrove Butler
Associate Administrator, Office of Financial Assistance

Joseph Loddo
Chief Financial Officer

From: Robert G. Seabrooks 
Assistant Inspector General for Auditing

Subject: Audit of 7(a) Service Fee Collections

BACKGROUND

Through the 7(a) loan program, the U.S. Small Business Administration (SBA) guarantees loans made to small businesses by participating lenders. For loans approved after October 12, 1995, lenders are required to pay SBA a yearly service fee equal to 0.5 percent of the outstanding balance of the guaranteed portion of each loan. Lenders remit the fees on a monthly basis, along with SBA Form 1502 – Guaranty Loan Status & Lender Remittance Form, to Colson Services Corporation (Colson), SBA's collection agent. Colson in turn remits the fees to SBA's Denver Finance Center. SBA records indicate that for the period October 1995 to May 1999, the agency was due about \$105 million in service fees on 140,165 loans.

Although lenders are required to submit loan balance information each month, SBA does not use those submissions to calculate fees due. Instead, it relies on: (a) lenders to calculate and remit the fees due¹ and (b) Colson to verify the accuracy of fees remitted based on the lender's monthly SBA Form 1502. The Office of Financial Assistance and the Office of the Chief Financial Officer are jointly responsible for oversight and collection of 7(a) loan service fees.

¹ For secondary market loans, Colson calculates fees due based on the principal and interest payments passed through by the lenders.

Objective and Scope

The audit objective was to determine if SBA collected the 7(a) loan service fees it was due for the period October 1995 through April 1999. We performed two analyses on data files drawn from SBA's Loan Accounting System (LAS), and reviewed a sample of loans with significant differences between calculated fee amounts due and collected.

In the initial data file analysis, we calculated and compared fees due and collected for 78,586 "current" 7(a) loans. We calculated fees due based on the period of time since the initial disbursement date, and the average of (a) the total loan amount disbursed and (b) the outstanding balance at the time of the analysis. We calculated fees collected by totaling all transactions for each loan recorded using the "fee collection" transaction code.

To find the reasons for differences between calculated amounts due and collected, we randomly selected 30 out of 129 loans with differences of more than \$2,500. For each sample loan, we analyzed lender transcripts, Colson records, and detailed SBA transaction files.

Based on the sample results, we refined our analysis methodology, and calculated and compared fees due and collected for 140,105 loans of all status types (e.g., current, paid-in-full, and charged-off). In the revised analysis, we calculated fees due based on a time-weighted average of all reported loan balances, and calculated fees collected based only on fee collection transactions that affected cash.

Fieldwork was performed at SBA Headquarters in Washington, D.C. between December 1998 and October 1999. The audit was conducted in accordance with government auditing standards.

AUDIT RESULTS

Overall, the audit showed that SBA collected the 7(a) service fees it was due through April 1999 for 95.5 percent of the 140,165 loans approved after October 12, 1995, but that it may not have collected as much as \$4.1 million for 4.5 percent of those loans. In addition, errors in SBA records precluded accurate calculation of fees due and collected, incorrectly indicating fee overpayments on 5.5 percent of the loans.

SBA was not able to ensure the collection of fees due for all loans and the accuracy of its records, because it did not have procedures in place to (a) calculate amounts due for comparison with amounts collected, and (b) follow up with lenders on loans with significant differences. It did, however, have the information necessary to implement such procedures. The loan balance information lenders are required to submit each month could be used to calculate fees due and establish receivable accounts. Using materiality thresholds and aging techniques, the receivable accounts could be used to identify and correct both fee collection errors, as well as inaccurate records.

1. Initial Analysis of Current Loans

The initial analysis of data files from SBA's loan accounting system, comparing fee amounts due and collected on "current" loans only, indicated the agency collected the fees due for almost 90 percent of the loans covered. For the remaining 10 percent, the analysis identified differences of more than \$250 between calculated amounts due and collected – both overpayments and underpayments.² The calculated overpayments totaled about \$2.6 million, and the calculated underpayments totaled about \$3.0 million.

2. Sample Results for Loans with Differences Greater than \$2,500

The sample of 30 loans contained 21 with calculated underpayments totaling \$62,500, and 9 with calculated overpayments totaling \$60,800. Detailed review of lender transcripts and SBA records showed that in most cases, calculated underpayments resulted from actual underpayments, while calculated overpayments resulted from inaccurate SBA records, as discussed below (see Attachment 1 for loan specific details).

- For 19 loans, SBA did not collect fees due totaling \$65,174. The lenders either did not set up the loans for fee payments or miscalculated amounts due. In one instance, after we contacted the lender, it lender identified additional fees payable of \$18,284 on the remaining SBA loans in its portfolio.
- For 8 loans, SBA collected the fees due, but inaccurate SBA records caused errors in the calculation of fees due and collected. These inaccurate records involved (a) incorrect initial disbursement dates – five loans; (b) incorrect use of the fee collection transaction code – two loans; and (c) fee collections applied to the wrong loan – one loan. The inaccurate records were caused by lenders' non-compliance with SBA reporting requirements and data entry errors.
- For 2 loans, SBA collected \$3,088 more than it was due. One case involved duplicate fee payments made by the lender and by Colson on a secondary market loan. In the other case, the lender used an incorrect guarantee percentage and miscalculated fees due.
- For 1 loan, SBA collected the fees due, but an invalid assumption in the initial analysis on the timing of loan disbursements caused an error in the calculation of fees due. The loan was disbursed over a period of time, whereas, our analysis assumed loan was totally disbursed on the initial disbursement date.

The sample review showed that data file analysis is an effective technique for identifying loans with unpaid fees and inaccurate records. For 29 of the 30 sample loans, detailed review showed that the differences between calculated amounts due and collected involved either (a) fee collection errors or (b) inaccurate SBA records. Further, 18 of 19 calculated underpayments

² We considered differences of less than \$250 to be immaterial.

involved actual underpayments, but only 2 of 11 calculated overpayments involved actual overpayments.

The sample review also showed that the initial data file analysis did not accurately calculate (a) fees due on loans with sequential disbursements, and (b) fees collected on loans where the “fee collection” transaction code was used to record non-cash transactions. We, therefore, revised our analysis methodology to correct for such occurrences.

3. Revised Analysis of Loans of All Status Types

As in the initial analysis, the revised analysis of SBA records indicated the agency collected the fees due for 90 percent of the 140,165 loans covered. The revised analysis also indicated that for 10 percent (13,873) of the loans, the difference between calculated amounts due and collected was greater than \$250, with both overpayments and underpayments, as summarized in the following tables.

Calculated Overpayments

<u>Amount</u>	<u># of Loans</u>	<u>Total</u>
\$250 - \$500	4,430	\$1,544,922
\$500 - \$1,000	2,228	\$1,523,910
\$1,000 - \$2,500	863	\$1,276,737
\$2,500 - \$5,000	87	\$278,114
> \$5,000	25	\$178,402
Totals	7,633	\$4,802,085

Calculated Underpayments

<u>Amount</u>	<u># of Loans</u>	<u>Total</u>
\$250 - \$500	3,534	\$1,230,455
\$500 - \$1,000	1,806	\$1,237,282
\$1,000 - \$2,500	772	\$1,130,599
\$2,500 - \$5,000	108	\$358,786
> \$5,000	20	\$128,944
Totals	6,240	\$4,086,066

Based on the results of the sample review, these differences between calculated amounts due and collected reflect either: (a) actual overpayments or underpayments, or (b) inaccurate SBA records. Moreover, calculated overpayments are more likely to involve inaccurate SBA records, while calculated underpayments are more likely to involve actual underpayments.

Recommendations

We recommend the Chief Financial Officer in conjunction with the Associate Administrator for Financial Assistance, and Associate Administrator for Field Operations:

1. Establish receivable accounts for 7(a) loan service fees. The accounts should be updated monthly using reported loan balance and fee collection information.
2. Develop procedures and materiality thresholds for the receivable accounts to (a) identify loans with significant differences between amounts due and collected, (b) determine the cause and (c) implement corrective action.
3. Collect the \$65,000 in underpaid fees and refund the \$2,100 in overpaid fees identified on Attachment 1.
4. Using the data file (provided separately), request lenders with calculated underpayments totaling more than \$1,000 to review their SBA loan portfolios and remit any fees due, or submit loan transcripts to substantiate that the calculated underpayments are the result of inaccurate SBA records. (\$3.7 million of the \$4.1 million in calculated underpayments was associated with 623 lenders with calculated underpayments totaling more than \$1,000).

SBA Management Response

The Chief Financial Officer responded that effective management of servicing fees was an important issue and that they were focused on improving this process. The CFO also generally agreed with the report's recommendations and replied that it needed to coordinate with the Office of Financial Assistance (OFA) and the Office of Field Operations (OFO) to define specific roles and responsibilities for implementing the recommendations.

OIG Evaluation

The CFO's reply was responsive to the report and its recommendations.

* * * * *

The findings in this report are based on the auditors' conclusions, and the report recommendations are subject to review, management decision, and action by your office in accordance with existing Agency procedures for audit follow-up and resolution. Please provide your management decision on SBA Form 1824 Recommendation Action Sheet, also attached, within 30 days. This report may contain proprietary information subject to the provisions of 18 USC 1905. Do not release to the public or another agency without permission of the Office of Inspector General. Should you or your staff have any questions, please contact John McCreary, Audit Manager, at (202) 205-7204.

Attachments

AUDIT OF 7(A) SERVICE FEE COLLECTIONS

Loan No.	Results	Calculated Under (Over) Payment	Actual Amount Due
Fees Not Collected			
FOIA Ex. 4	Lender did not pay fees due 6/97 to 3/98.	\$2,586	\$2,266
FOIA Ex. 4	Lender did not pay fees due 6/97 to 1/99.	\$3,647	\$5,068
FOIA Ex. 4	Lender did not pay fees due 7/97 to 1/99.	\$3,790	\$3,529
FOIA Ex. 4	Lender did not pay fees due 10/95 to 8/96.	\$4,147	\$5,218
FOIA Ex. 4	Lender did not pay fees due 11/95 to 6/96 and 8/96 to 1/99.	\$3,460	\$3,952
FOIA Ex. 4	Lender did not pay fees due 7/96 to 1/99.	\$2,554	\$2,289
FOIA Ex. 4	Lender did not pay fees due 12/95 to 12/96.	\$3,027	\$751
FOIA Ex. 4	Lender did not pay fees due 11/96 to 10/98.	\$3,076	\$3,700
FOIA Ex. 4	Lender did not pay fees due 12/95 to 10/96.	\$3,514	\$3,654
FOIA Ex. 4	Lender did not pay fees due 2/96 to 8/97.	\$2,724	\$2,775
FOIA Ex. 4	Lender did not pay fees due 12/95 to 4/97.	\$3,159	\$3,177
FOIA Ex. 4	Lender did not pay fees due 4/96 to 10/96.	\$1,815	\$1,264
FOIA Ex. 4	Lender did not pay fees due 1/96 to 12/97.	\$2,512	\$1,628
FOIA Ex. 4	Lender did not pay fees due 12/96 to 6/98 and 7/98 to 1/99.	\$2,941	\$1,523
FOIA Ex. 4	Lender did not pay fees due 3/97 to 1/99.	\$4,082	\$5,478
FOIA Ex. 4	Lender did not pay fees due 4/97 to 3/98 and 6/98 to 1/99.	-\$3,220	\$2,492
FOIA Ex. 4	Lender did not pay fees due 1/97 to 6/98.	\$4,973	\$4,865
FOIA Ex. 4	Lender did not pay fees due for the period 8/97 to 1/99.*	\$3,779	\$5,603
FOIA Ex. 4	Lender did not pay fees due for the period 4/97 to 1/99.	<u>\$3,569</u>	<u>\$5,942</u>
Total		<u>\$56,136</u>	<u>\$65,174</u>

* Lender identified additional fees due totaling \$18,284 on the remaining SBA loans in its portfolio.

AUDIT OF 7(A) SERVICE FEE COLLECTIONS

Loan No.	Results	Calculated Under (Over) Payment	Actual Amount Due
Fees Collected / Inaccurate Records			
FOIA Ex. 4	Incorrect initial disbursement date in SBA records caused understatement of fees due.	(\$2,591)	\$0
FOIA Ex. 4	Incorrect use of transaction code for fee collections caused overstatement of fees collected.	(\$24,861)	\$0
FOIA Ex. 4	Fee payments for another loan were incorrectly applied to this loan resulting in apparent overpayment.	(\$2,806)	\$0
FOIA Ex. 4	Incorrect use of transaction code for fee collections caused overstatement of fees collected.	(\$5,013)	\$0
FOIA Ex. 4	Incorrect initial disbursement date in SBA records caused understatement of fees due.	(\$3,936)	\$0
FOIA Ex. 4	Incorrect initial disbursement date in SBA records caused understatement of fees due.	(\$4,654)	\$0
FOIA Ex. 4	Incorrect initial disbursement date in SBA records caused understatement of fees due.	(\$3,770)	\$0
FOIA Ex. 4	Incorrect initial disbursement date in SBA records caused understatement of fees due.	<u>(\$2,938)</u>	<u>\$0</u>
Total		<u>(\$50,569)</u>	<u>\$0</u>
Fees Overpaid			
FOIA Ex. 4	Lender overpaid fees from 6/96 to 1/99 due to incorrect guarantee percentage and calculation error. Incorrect SBA loan balance records caused understatement of fees due.	(\$3,651)	(\$995)
FOIA Ex. 4	Lender duplicated fee payments made by Colson 9/96 to 8/97.	<u>(\$3,358)</u>	<u>(\$2,093)</u>
Total		<u>(\$7,010)</u>	<u>(\$3,088)</u>
Invalid Disbursement Assumption			
FOIA Ex. 4	Loan was disbursed sequentially, causing over statement of fees due.	<u>\$3,129</u>	<u>\$0</u>
Total		<u>\$3,129</u>	<u>\$0</u>



U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

Attachment 2

Date: MAR 30 2000
To: Robert G. Seabrooks, Assistant Inspector General for Auditing
From: Joseph P. Loddo, Chief Financial Officer
Cc: Jane Butler, Associate Administrator for Field Operations
Robert Baskin, Associate Administrator for Field Operations

Subject: Audit of 7(a) Service Fee Collections

The Office of the Inspector General's (OIG) draft audit report "Audit of 7(a) Fee Collections" was issued to the Office of the Chief Financial Officer (OCFO) on February 15, 2000. First of all, I want to thank you for conducting this review and extending our time to respond. The effective management of servicing fees is an important issue to us, and we are focused on improving this process. I was pleased that you noted in the audit that the servicing fees due to SBA were received on 95 percent of our 7(a) loans. This good record has been achieved through close management attention to this area. However, it was also important for you to note that up to \$4.1 million of loan servicing fees may not have been collected, and this means we need to continue our close monitoring of this area and can probably do even more.

As discussed in your report, the proper management of servicing fees involves the following SBA offices:

- OCFO deposits and records servicing fees initially received by Colson, our fiscal agent,
- Office of Financial Assistance (OFA) oversees Colson's fee collections and record keeping,
- Office of Field Operations (OFO) oversees field office activity.

Because these offices are jointly responsible for the establishment of policy on servicing fees and because all of their support is required to act on your recommendations, we recommend that your final audit report should be addressed to all three offices rather than solely to my office so that appropriate management attention is provided by all three responsible offices.

Although we generally agree with the report's recommendations, because these other offices must be involved in their implementation, we still need to coordinate with them regarding specific roles and responsibilities to address your recommendations. We will work closely with OFA, OFO and OIG to resolve those issues during the audit follow-up process.

Thank you again for your work on this important area. I can assure you that the SBA is committed to the effective management of its loan servicing fees, and that we will address the recommendations in your final audit report in a timely and efficient manner.

REPORT DISTRIBUTION

<u>Recipient</u>	<u>No. of Copies</u>
Deputy Administrator	1
Chief Information Officer	1
General Counsel.....	2
Director of Secondary Markets & 504, Office of Financial Assistance.....	1
U.S. General Accounting Office	1